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Supreme Court, U.S.
FILED
DEC 3 1987
JOSEPH F. SPANIOL, JR.
CLERK

No. 87-343

In The
Supreme Court of the United States
October Term, 1987

STATE OF MONTANA; JOHN D. LaFAVER, Director, Montana Department of Revenue; BIG HORN COUNTY, Montana; TREASURE COUNTY, Montana; YELLOWSTONE COUNTY, Montana; LORRAINE HAMILTON, Treasurer, Big Horn County, Montana; KATHLEEN THOMAS, Treasurer, Treasure County, Montana; and MAY JENKINS, Treasurer, Yellowstone County, Montana,

Appellants,

vs.

CROW TRIBE OF INDIANS; UNITED STATES OF AMERICA; and WESTMORELAND RESOURCES, INC.,

Appellees.

ON APPEAL FROM THE NINTH CIRCUIT COURT OF APPEALS

APPELLANTS' REPLY BRIEF

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APPELLANTS' REPLY BRIEF

Appellees Crow Tribe of Indians and United States have filed separate motions to affirm the court of appeals' judgment. Both motions obscure the critical fact that the Montana coal gross proceeds tax, Mont. Code Ann. §§ 15-23-701 to -704 (1987), and the Montana coal severance tax, Mont. Code Ann. §§ 15-31-101 to -205 (1987), are imposed not on the Tribe but on appellee Westmoreland Resources, Inc., a non-Indian producer, and that the taxes are calculated upon a value which is determined after ownership of the resource has passed from the Tribe to Westmoreland. The motions further ask the Court to credit a reading of the Act of May 19, 1958, 72 Stat. 121 (1958 Act), inconsistent with the express language of that statute and its legislative history. Finally, the United States' motion seeks to establish an extraordinarily broad range of federal preemption under the Indian Mineral Leasing Act of 1938, 52 Stat. 347 (*codified as amended in* 25 U.S.C. §§ 396a to 396g) (1938 Act), on the basis of isolated phrases from Senate Report No. 985, 75th Cong., 1st Sess. (1937). The motions to affirm thus underscore the substantial nature of the questions presented and the appropriateness of plenary consideration.

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ARGUMENT

1. The motions to affirm directly or indirectly characterize the challenged taxes as being imposed on the Tribe or its property.[1] Nonetheless, the court of appeals

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[1] The Tribe takes solace from the statement in *New Mexico v. Mescalero Apache Tribe*, 462 U.S. 324, 336 (1983), that "[t]he

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expressly held in *Crow Tribe v. Montana*, 650 F.2d 1101, 1110-11 (9th Cir. 1981), *amended*, 665 F.2d 1390, *cert. denied*, 459 U.S. 916 (1982) (J.S. App. 79a, 87a-90a), that the legal incidence of the state taxes falls on the producer, while the Montana Supreme Court has said that the act of severance effects a transfer of title to the coal from the mineral lessor to the lessee.[2] Instantly, that producer-lessee is Westmoreland which enjoys no statutory or common-law exemption from otherwise valid state taxation. *See, e.g., Mescalero Apache Tribe v. Jones*, 411 U.S. 145, 150-55 (1973) (refusing to recognize tribal entity doing business off-reservation as federal instrumentality to whom United States' immunity against state taxation attached); *Oklahoma Tax Commission v. Texas Co.*, 336 U.S. 342, 365 (1949) (overturning prior decisions which expansively applied intergovernmental immunity

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exercise of state authority which imposes additional burdens on a tribal enterprise must ordinarily be justified by functions or services performed by the State in connection with on-reservation activity." (Crow Motion 10.) The United States argues that Montana "seeks to impose its taxes on the extraction of minerals that are unquestionably the property of the Tribe and are held in trust by the United States" and that "[t]here can be little doubt that Montana is prohibited from imposing a real property tax on any lands, including coal deposits, that are held by the United States in trust for the Tribe[.]" (U.S. Motion 13.)

[2] In *Commonwealth Edison Co. v. Montana*, 189 Mont. 191, 211, 615 P.2d 847, 858 (1980), *aff'd*, 453 U.S. 609 (1981), the court rejected a contention that, by taxing coal derived from federal leases, the State effectively taxed the nation as a whole, commenting that, "[o]nce mined under a federal lease or permit, title to the coal is vested as personal property in the lessee or permittee as soon as it is mined and removed from its original place" and that "[t]he coal being taxed here . . . is not 'our' coal, but the personal property of the [lessee] who produced it under lease or permit."

doctrine to private persons and holding state gross production and excise taxes valid with respect to oil and gas production pursuant to lease under 1938 Act).

Not only does the legal incidence of the Montana taxes fall on Westmoreland as the lessee-producer, but the amount actually taxed is determined on the basis of the post-severance "contract sales price," i.e., the FOB mine price minus various statutory deductions. Mont. Code Ann. §§ 15-23-701(d), 15-35-102(5), 15-35-103. The FOB mine price derives from a variety of factors, including the cost of labor, operational productivity, the producer's desired rate of return, state and federal taxes, and royalty obligations. (Trial Ex. D-301 at Ex. V-2.) However, because the contract sales price excludes production taxes passed through by the producer to a buyer[3] and a portion of royalties paid to Montana, the United States or a federally recognized Indian tribe (Mont. Code Ann. § 15-35-102(5)), those elements constituting the taxable valuation are substantially controlled by the producer's entrepreneurial acumen in extracting and marketing the coal. The gross proceeds and severance taxes are accordingly based upon an economic value which is determined following transfer of ownership to Westmoreland and is devoid of contribution from tribal facilities or management. *Cf. California v. Cabazon Band of Mission*

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[3] Mont. Code Ann. § 15-35-102(13) defines "taxes paid on production" to include "any tax paid to the federal, state, or local governments upon the quantity of coal produced as a function of either the volume or the value of production and does not include any tax upon the value of mining equipment, machinery, or buildings and lands, any tax upon a person s net income derived in whole or in part from the sale of coal, or any license fee." (J.S. App. 212a.)

Indians, 107 S. Ct. 1083, 1093-94 (1987) (tribes provided modern facilities for gaming establishments operated on reservation). The very method by which taxable value is calculated directly militates against the Tribe and United States' effort to portray the taxes as being imposed on trust property.

2. Both motions to affirm contend that the 1958 Act applies to mineral interests reserved by the United States when ceded-strip surface estates were conveyed. (Crow Motion 7; U.S. Motion 4, 13.) They also state that Montana does not "seriously challenge" (Crow Motion 9) or "appear to challenge" (U.S. Motion 13) this conclusion. Quite obviously, though, Montana has attacked that construction of the 1958 Act, terming it "radically skewed" (J.S. 17) because the Act facially refers to vacant and undisposed-of surface lands and the associated legislative history is silent as to restoration of mineral interests. *See* S. Rep. No. 1508, 85th Cong., 2d Sess. (1958) (J.S. App. 249a-256a). Had Congress intended to restore mineral interests under surface lands unaffected by the statute, it would presumably have said so.[4]

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[4] In the face of congressional silence, the United States argues that the 1958 Act was intended to extend to tribes which had not accepted the provisions of the Indian Reorganization Act of 1934, 48 Stat. 984 (*codified in* 25 U.S.C. §§ 461 to 479), the benefits accorded under the IRA. (U.S. Motion 3-4.) Equality, however, did not require such extension here since, under the Court's reasoning in *Ash Sheep Co. v. United States*, 252 U.S. 159, 166 (1920), the Tribe retained a beneficial ownership interest in all ceded-strip reserved minerals and that interest was already protected under the 1938 Act. In the latter regard,

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Yet, even were the Tribe and United States' premise concerning the effect of the 1958 Act on reserved mineral interests underlying nonrestored surface lands valid, analytical difficulties abound. The United States, for example, admits in its motion that the 1958 Act did not "expand the exterior boundaries of the Crow Reservation on the surface or . . . confer civil or criminal jurisdiction on the Tribe as a general matter." (U.S. Motion 24.) If, however, the Crow Reservation's exterior boundaries were not modified with respect to surface lands by the Act, there can be no logical claim that those boundaries were somehow extended subsurfacely. Perhaps recognizing the inherent contradiction in its position, the United States suggests that it is unimportant whether Westmoreland's mining activities occur on "reservation" lands since, under any circumstances, the 1938 Act applies. (*Id.* at 23.) Nonetheless, *Mescalero Apache Tribe v. Jones, supra,* unquestionably has continuing vitality (*New Mexico v. Mescalero Apache Tribe,* 462 U.S. at 335 n.18), and the locus of the regulated activity thus has particular significance here because, when outside a reservation's exterior boundaries, no exemption from state taxation

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it should be noted that the exclusion of the "Crow Reservation" in section 6 of the 1938 Act, 25 U.S.C. § 369f, did not apply to reserved mineral interests under the ceded strip because they were not part of the Reservation; a contrary conclusion, moreover, would preclude application of the 1938 Act to the ceded-strip interests presently at issue since they do not underlie lands available for allotment pursuant to the Act of June 4, 1920, 44 Stat. 751, 753 (J.S. App. 161a, 162a-163a), as amended, and were therefore unaffected by the Act of September 16, 1959, 73 Stat. 565 (J.S. App. 181a), extending coverage of the 1938 Act to such lands.

can be conferred upon tribal entities without an express congressional mandate. *Jones* compels at least as stringent a rule with respect to non-Indian mineral lessees.[5] There is, of course, no express exemption from state taxation in either the 1958 Act or any other federal statute presently applicable, and the United States thus effectively requests the Court to adopt an analysis at odds with the dichotomy drawn in *Jones*.[6]

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[5] The United States relies on *British-American Oil Producing Co. v. Board of Equalization*, 299 U.S. 159 (1936), for the proposition that *any* taxation of a non-Indian mineral lessee requires explicit congressional consent. (U.S. Motion 15-16.) This argument is premised on the Court's statement that "[t]he taxes in question are a gross production tax and a net proceeds tax, and it is conceded that the State is without power to apply either to the production under this lease, save and except as Congress may have given its assent." *Id.* at 161. Nevertheless, not only did *British-American* involve production within the exterior boundaries of the Blackfeet Reservation, but the concession conclusorily referred to can hardly be metamorphosed into a holding. Moreover, were the importance attached to this aspect of the decision by the United States accepted, an obvious conflict would arise with respect to the later-decided *Oklahoma Tax Comm'n v. Texas Co., supra*, which rejected the federal instrumentality doctrine upon which the concession was apparently based. *See British-American Oil Producing Co. v. State Board of Equalization*, 101 Mont. 293, 296, 54 P.2d 129, 130, *aff'd*, 299 U.S. 159 (1936).

[6] The United States contends *Jones* is consistent with its position because that decision struck down a state compensating use tax on materials used to construct ski lifts on trust land and because "a tax on the extraction of tribally owned minerals likewise is effectively a tax on the trust land itself." (U.S. Motion 25-26.) This contention ignores the fact that the Montana taxes are imposed not on "the trust land itself" but on an economic value determined after severance and transfer of ownership from the mineral lessor to the lessee and that, in *Jones*, an explicit exemption from state and local taxation existed under 25 U.S.C. § 465 for the lands to which the ski lifts were deemed fixtures—an exemption unavailable to the Tribe since the mineral interests at issue were not acquired under the IRA.

3. The United States' motion to affirm discusses at length the 1938 Act's preemptive scope and argues, in essence, that any state taxation of non-Indian producers like Westmoreland is foreclosed, irrespective of whether on- or off-reservation, unless the tax revenues bear a direct relationship to the cost of governmental services provided the producer in connection with the taxed activity. (U.S. Motion 14-22.) Its argument is predicated principally on the notion that the 1938 Act is intended "to ensure that Indians receive 'the greatest return from their property[.]' " (*Id.* at 16.)[7]

To the extent the United States' position is urged as to mining activity concededly outside the exterior boundaries of the Crow Reservation, it squarely conflicts with *Jones* for those reasons stated above. Furthermore, even if *Jones* is placed aside, its position glosses over the admitted fact that, unlike *White Mountain Apache Tribe v. Bracker*, 448 U.S. 136 (1980), or later cases, the ceded

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[7] The United States additionally argues that the Montana taxes "conflict with the policy of the 1938 Act to 'bring all mineral-leasing matters in harmony with the Indian Reorganization Act' " because they run counter to the IRA's "repudiation of the allotment and surplus-land policies" previously in effect (U.S. Motion 17-18.) The reference in Senate Report No. 985, 75th Cong., 1st Sess. (1937), to bringing all "mineral-leasing matters in harmony with the Indian Reorganization Act" was, however, clearly directed to giving tribes control over the leasing of their mineral resources, which did not then exist under all federal statutes but which was provided under the IRA. Moreover, not only is the 1938 Act silent on the question of state taxation, but the IRA also does not address the authority of states to tax non-Indians. The United States' more general contention that the taxes offend the IRA's purpose of facilitating tribal economic development (U.S. Motion 18-19) has been rejected in *Jones*, 411 U.S. at 150-53, and *Washington v. Confederated Tribes of Colville Ind. Res.*, 447 U.S. 134, 155 (1980).

strip is governmentally administered by Montana and various state political subdivisions. The very underpinning of *White Mountain*—state taxation of activities as to which Arizona had little or no responsibility—is thus absent here. *See Washington v. Confederated Tribes of Colville Indian Reservation*, 447 U.S. at 162 (upholding state's authority to seize tribally-owned unstamped cigarettes and finding significant "that these seizures take place outside the reservation, in locations where state power over Indian affairs is considerably more expansive than it is within reservation boundaries"). It is instead the Tribe which has no governmental responsibility but which seeks to exclude Montana from imposing taxes uniformly required of producers like Westmoreland.[8] To

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[8] As the district court stated, the Tribe's severance tax code was not approved by the Secretary of the Interior for application to the ceded strip "because the Tribe lacks the power under its constitution to levy a tax off its reservation and because the Secretary has not determined whether such power exists as a matter of federal law." (J.S. App. 53a.) The absence of such authority parallels the Tribe's lack of governmental responsibility for the ceded strip and distinguishes this matter from the *White Mountain* paradigm where a state attempts to assert its taxing or regulatory power in a geographical area and over a relationship largely outside its control as sovereign. It must be emphasized that the 1982 lease amendment providing for the payment of a "tax" by Westmoreland to the Tribe under certain conditions is not contrary to the latter's lack of tax authority on the ceded strip. The amendment provided that Westmoreland would pay to the Tribe "a tax equal to the Montana State Coal Severance Tax . . . applicable to the mining of coal generally within the state . . . and a tax equal to the Montana State Gross Proceeds Tax . . . applicable to the mining of coal generally within the state . . . less whatever amount is required to be paid in severance and gross proceeds taxes to the State of Montana or its political subdivisions." (Trial Ex. P-81 at 1-2.) Despite use of the term "tax," the agreement also stated that

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construe an isolated phrase in the Acting Secretary of the Interior's letter reproduced in Senate Report 985 as mandating adoption of the preemption standard espoused by the court of appeals, Tribe and United States does noting more than judicially legislate. Unquestionably, the issue of whether *White Mountain* interest-balancing standards apply here and, if so, how they should be applied demands a far more careful analysis than that suggested below or by the Tribe and United States.[9]

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the amendment "will not be construed in any way as an admission by Lessee that Lessor has any power to impose any tax on Lessee without Lessee's consent." (*Id.* at 3.) The "tax" is thus a consensual arrangement and not the Tribe's unilateral exercise of sovereign authority. *See Merrion v. Jicarilla Apache Tribe*, 455 U.S. 130, 147 (1982) ("[w]hatever place consent may have in contractual matters and in the creation of democratic governments, it has little if any role in measuring the validity of an exercise of legitimate sovereign authority").

[9] The facile nature of their analysis, wholly accepted by the court of appeals, is reflected in its two major tenets. First, the notion that a *quid pro quo* relationship must exist between tax revenues received and services rendered distorts *White Mountain*, which did not limit the scope of legitimate state interests to simply recouping identifiable expenditures. *White Mountain* instead requires substantially greater attention and weight be given to the involved governmental realities. Second, the Tribe and United States' implicit assertion that courts are equipped to make difficult policy decisions with respect to appropriate taxation levels—especially when, as the district court found (J.S. App. 43a-45a, 52a-53a), many future governance costs are unquantifiable, is highly questionable. *See Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 629 (1981) ("it is doubtful whether any legal test could adequately reflect the numerous and competing economic, geographic, demographic, social, and political considerations that must inform a decision about an acceptable rate or level of state taxation, and yet be reasonably capable of application in a wide variety of individual cases").

CONCLUSION

The appellants respectfully request that the motions to affirm be denied, that probable jurisdiction be noted, and that plenary briefing and argument on the merits be ordered.

Respectfully submitted,

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December 1987